ST 03-10
Tax Type: Sales Tax

Issue: Tangible Personal Property

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS

THE DEPARTMENT OF REVENUE	)	Docket No. 01-ST-0000
OF THE STATE OF ILLINOIS	)	IBT No. 0000-0000
v.	)	NTL No. SF 00000000000001
"STRATOSPHERE AVIATION, INC.",	)	Assmt. No. SB 00000000000002
d/b/a "Go Anywhere Aviation Services",	)	
formerly "Creative Aviation Services, LP",	)	John E. White,
Taxpayer	)	Administrative Law Judge

RECOMMENDATION FOR DISPOSITION

Appearances: Fred Marcus, Horwood Marcus & Berk, appeared for "Stratosphere Aviation, Inc."; John Alshuler, Special Assistant Attorney General, appeared for the Illinois Department of Revenue.

Synopsis: This matter arose after "Stratosphere Aviation, Inc.", doing business as "Go Anywhere Aviation Services," ("GAAS" or "Taxpayer) protested a Notice of Tax Liability ("NTL") and an additional assessment the Illinois Department of Revenue ("Department") issued to it. During the audit years, "GAAS" was owned by "Creative Aviation Services, LP" ("CAS"), a Delaware limited partnership. The NTL and assessment assessed Illinois Service Occupation Tax ("SOT") and other taxes against taxpayer, and were issued following the Department's audit of "GAAS" for the monthly periods beginning July 1, 1994 through and including May 31, 1996.

In lieu of hearing, the parties submitted this matter upon a stipulation of facts and their submission of stipulated exhibits. The major issue is whether "GAAS's" cost price

of tangible personal property (hereinafter, "goods") that it transferred to others incident to its sales of aircraft retrofit service, was exempt from SOT, pursuant to § 3-45 of the Service Occupation Tax Act ("SOTA"). Two other issues are: whether "GAAS" is liable for tax based on its cost price of goods it purchased and installed either on other's aircraft or on aircraft engines in Illinois, pursuant to an Operating Agreement with Allied Signal, Inc.; and, if so, whether the Department properly calculated the amount of tax due regarding such transactions. After considering the evidence submitted, I am making findings of fact and conclusions of law. I recommend that the issues be resolved in favor of the Department.

Findings of Fact:

Facts Regarding the Department's Audit and The NTL

1. The assessments arise out of various services "GAAS" performed during the months of July 1, 1994 through and including May 31, 1996, at its hangar facilities located in "Someplace", Illinois. Stip. ¶¶ 2, 17, 20; Stip. Ex 1 (copy of NTL and assessment).

2. During the audit period, "GAAS" performed a variety of services for owners of business aircraft. Stip. ¶ 18. These services included: the complete disassembly, repair, re-assembly, and functionality testing of aircraft engines; the service and repair of aircraft airframes, avionics, and aircraft interiors; and retrofits of business jet aircraft. *Id*. A basic retrofit of an aircraft involves the replacement of the original engines on the aircraft with new/improved engines and the installation of new pylons, nacelles, and associated wiring, plumbing, and cockpit instrumentation necessary to accommodate the new engines. *Id*.

3. "GAAS" held Air Agency Certificate U0000001, issued by the Federal Aviation Administration ("FAA") on January 3, 1978 and reissued on July 29, 1998 Stip. ¶ 115; Stip. Ex. 84 (copy of certificates). The certificate authorized "GAAS" to operate a repair station with the following ratings: Accessory, Airframe, Powerplant, Radio, Instrument, and later, Limited Nondestructive Testing, and Limited Propeller. Stip. Ex. 84, p. 1. The certificate provided, in part:

> a. These operations specifications are issued [to "GAAS"] … pursuant to Title 14 Code of Federal Regulations (CFR) Section 145.11. The repair station certificate holder shall conduct operations in accordance with CFR Part 145 and these operations specifications.
>
> ***
>
> d. The repair station specified on these operations specifications is performing maintenance and/or alteration of aircraft and/or aeronautical products to be installed on aircraft under the terms and conditions of a Bilateral Aviation Safety Agreement and associated Maintenance Implementation Procedures between the [FAA] and Joint Aviation Authority member countries.

Stip. Ex. 84, p. 4 (§ A001(a), (d)).

4. When an aircraft undergoes a basic retrofit, the customer is also given the option to obtain upgraded avionics, auxiliary power units and thrust reversers, and to have the interior and exterior of the aircraft refurbished while it is undergoing the engine retrofit. Stip. ¶ 19.

5. On December 29, 2000, and as a result of its audit, the Department timely issued a Notice of Tax Liability ("NTL") assessing additional service occupation tax ("SOT") in the amount of $5,510,495, which included tax in the amount of $3,767,237, and interest in the amount of $1,743,258. Stip. ¶ 21; Stip. Ex. 1 (copy

of NTL and of form SC-10-K, Audit Correction and/or Determination of Tax Due).

6. The additional tax arises from "GAAS's" transfer of tangible personal property to different aircraft owners as an incident to performing the following services:

(a) Services performed in "Someplace", Illinois on aircraft that were subsequently delivered to their owners at out-of-state locations.

(b) "Maintenance Service Plan" work performed on aircraft at the direction of "American Signcraft"; and

(c) Maintenance and repair work performed on loaner/rental engines owned by "American Signcraft" at the direction of "American Signcraft".

Stip. 23.

7. On February 26, 2001, "GAAS's" owner, "Garfield Utility Company", timely protested the NTL. Stip. ¶ 24; Stip. Ex. 2 (copy of protest).

8. "GAAS" performed 11 (eleven) retrofits for customers during the audit period. Stip. ¶¶ 26, 35, 45, 51, 56, 61, 67, 75, 81, 87, 93.

9. For each of the retrofits, "GAAS" installed, but did not transfer, new aircraft engines onto a customer's aircraft. Stip. Ex. 82, p. 6; 35 **ILCS** 115/2 ("transfer" being "any transfer of the title to property or of the ownership of property whether or not the transferor retains title as security for the payment of amounts due him from the transferee"). Each customer purchased the engines "GAAS" installed directly from "American Signcraft", the manufacturer, and "GAAS" billed each customer for engine installation services, in addition to its charges for the goods it did transfer incident to its sales of services. Stip. Ex. 82, p. 6.

"GAAS's" Retrofit of "Unified Slope Wing" Aircraft Bearing Serial Number 001

10. Between June 22, 1994 and December 21, 1994 "GAAS" performed an engine retrofit on "Unified Slope Wing Aircraft" ("USWA") Falcon 20 aircraft bearing serial number 001 at its "Someplace, Illinois hangar facility. Stip. ¶ 26.[1]

11. "USWA" also elected to have its aircraft's avionics updated and certain maintenance work performed when "GAAS" was performing the retrofit. Stip. ¶ 29.

12. Upon completion of the retrofit work, "GAAS" personnel, pursuant to an agreement between "GAAS" and "USWA", on December 21, 1994, flew "USWA's" aircraft to a location outside the State of Illinois at which location "USWA" took custody and control of the aircraft from "GAAS". No "USWA" employees or representatives were present on the flight. Stip. ¶ 32.

13. "USWA's" aircraft returned to "GAAS's" "Someplace", Illinois location on the dates and for the purposes, indicated below.

Work Order	Date	Description of Service
33-0000	5/95	Warranty work
70-0000	7/95	Install dual GNS/XLS
33-0000	7/95	Warranty work

Stip. ¶ 33.

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[1] Pursuant to § 10-40 of the Illinois Administrative Procedures Act ("IAPA"), Stipulation Exhibits 3 through 78, consisting of "GAAS's" invoices for the retrofits at issue and/or "GAAS's" retrofit warranty work, are stricken from this record because they are unduly repetitious of the facts to which the parties stipulated. Stip. ¶¶ 18-19, 23, 26, 35, 45, 51, 56, 61, 67, 75, 81, 87, 93; 5 **ILCS** 100/10-40 ("[i]rrelevant, immaterial, or unduly repetitious evidence shall be excluded."); Transcript of Parties' Submission of Stipulated Record, p. 3 (parties advised that ALJ would retain discretion to strike exhibits submitted, pursuant to the IAPA). The parties do not dispute that "GAAS" installed the goods detailed on the invoices into or onto customers aircraft in Illinois, and neither party cited to any of these documents to support any other fact or any argument presented in their initial briefs.

"GAAS's" Retrofit of "USWA's" Aircraft Bearing Serial Number 002

14. Between July 7, 1994 and December 30, 1994 "GAAS" performed an engine retrofit on "USWA's" Falcon 20 aircraft bearing serial number 002 at its "Someplace", Illinois hangar facility. Stip. ¶ 35.

15. "USWA" elected to have "GAAS" update the aircraft's avionics and perform certain maintenance work. Stip. ¶ 38.

16. Upon completion of the retrofit work, "GAAS" personnel, pursuant to an agreement between "GAAS" and "USWA", on December 30, 1994, flew "USWA's" aircraft to a location outside the State of Illinois at which location "USWA" took custody and control of the aircraft from "GAAS". No "USWA" employees or representatives were present on the flight. Stip. ¶ 42.

17. "USWA's" aircraft returned to "GAAS's" "Someplace", Illinois location on the dates and for the purposes, indicated below:

Work Order	Date	Description of Service
33-0000	6/95	Warranty work
70-0000	7/95	Install GNS/XLS

Stip. ¶ 43.

"GAAS's" Retrofit of "USWA's" Falcon 20 Aircraft Bearing Serial Number 003

18. Between February 28, 1995 and October 4, 1995 "GAAS" performed an engine retrofit and various other services on "USWA's" Falcon 20 aircraft bearing serial number 003 at its "Someplace", Illinois facility. Stip. ¶ 45.

19. Upon the completion of the retrofit work, "GAAS" personnel, pursuant to an agreement between "GAAS" and "USWA", flew "USWA's" aircraft to a location

outside the State of Illinois at which location "USWA" took custody and control of the aircraft from "GAAS". No "USWA" employees or representatives were present on the flight. Stip. ¶ 48.

20. "USWA's" aircraft returned to "GAAS's" "Someplace", Illinois location on the dates and for the purposes indicated below:

RPA	Date	Description of Service
0000	11/95	Warranty repair
0000	12/95	Maintenance
0000	1/96	Warranty repair

Stip. ¶ 49 ("RPA" means a monthly sales dispatched query. Stip. ¶ 5.).

"GAAS's" Retrofit of "USWA's" Falcon 20 Aircraft Bearing Serial Number 004

21. Between July 3, 1995 and January 19, 1996 "GAAS" performed an engine retrofit and various other services on "USWA's" Falcon 20 aircraft bearing serial number 004 at its "Someplace", Illinois facility. Stip. ¶ 51.

22. Upon completion of the retrofit and other work "GAAS" performed on the aircraft, "GAAS" personnel, pursuant to an agreement between "GAAS" and "USWA", flew "USWA's" aircraft to a location outside the State of Illinois at which location "USWA" took custody and control of the aircraft from "GAAS". No "USWA" employees or representatives were present on the flight. Stip. ¶ 54.

"GAAS's" Retrofit of "Carnivale Flying Services" Aircraft Bearing Serial Number 005

23. Between July 31, 1995 and January 3, 1996 "GAAS" performed an engine retrofit and various other services on "Carnivale Flying Service's" ("CFS") Falcon 20 aircraft bearing serial number 005 at its "Someplace", Illinois facility. Stip. ¶ 56.

24. Upon completion of the retrofit work, "GAAS" personnel, pursuant to an agreement between "GAAS" and "CFS", flew "CFS's" aircraft to a location outside Illinois, at which location "CFS" took custody and control of the aircraft from "GAAS". No "CFS" employees or representatives were present on the flight. Stip. ¶ 59.

"GAAS's" Retrofit of "ABC/XYZ's Aircraft Bearing Serial Number 006

25. Between June 26, 1995 and October 5, 1995 "GAAS" performed an engine retrofit and avionics work on "ABC/XYZ's Falcon 20 aircraft bearing serial number 006 at its "Someplace", Illinois facility. Stip. ¶ 61.

26. Upon completion of the retrofit work, "GAAS" personnel, pursuant to an agreement between "GAAS" and "ABC/XYZ", flew "ABC/XYZ's aircraft to a location outside Illinois, at which location "ABC/XYZ" took custody and control of the aircraft from "GAAS". No "ABC/XYZ" employees or representatives were present on the flight. Stip. ¶ 64.

27. "ABC/XYZ's" aircraft returned to "GAAS's" "Someplace", Illinois facility on the date and for the purpose indicated below:

RPA	Date	Description of Service
000	12/95	Warranty repair

Stip. ¶ 65.

"GAAS's" Retrofit of "Baker Industrial's" Aircraft Bearing Serial Number 007

28. Between April 22, 1994 and October 22, 1994 "GAAS" performed an engine retrofit and various other services on "Baker Industrial's" Falcon 20 aircraft bearing serial number 007 at its "Someplace", Illinois facility. Stip. ¶ 67.

29. Upon completion of the retrofit work, "GAAS" personnel, pursuant to an agreement between "GAAS" and "Baker Industrial", flew "Baker Industrial's" aircraft to a location outside the State of Illinois at which location "Baker Industrial" took custody and control of the aircraft from "GAAS". No "Baker Industrial" employees or representatives were present on the flight. Stip. ¶¶ 70-71.

30. "Baker Industrial's" aircraft returned to the "Someplace", Illinois on the dates and for the purposes indicated below:

Work Order	Date	Description of Service
33-0000	7/95	Airframe warranty
48-0000-01	7/95	Warranty repairs
48-0002	9/95	Warranty repairs
48-0003	11/94	Warranty repairs
33-0001	12/94	Warranty repairs

Stip. ¶ 73.

"GAAS's" Retrofit of "Risk Asset Corp.'s" Aircraft Bearing Serial Number 008

31. Between August 8, 1994 and January 30, 1995 "GAAS" performed an engine retrofit and various other services on "Risk Asset Corp.'s" Falcon 20 aircraft bearing serial number 008 at its "Someplace", Illinois facility. Stip. ¶ 75.

32. Upon completion of the retrofit work, "GAAS" personnel, pursuant to an agreement between "GAAS" and "Risk Asset", flew "Risk Asset's" aircraft to a location outside the State of Illinois at which location "Risk Asset" took custody and control of the aircraft from "GAAS". No "Risk Asset" employees or representatives were present on the flight. Stip. ¶ 78.

33. "Risk Asset Corp.'s" aircraft returned to "GAAS's" "Someplace", Illinois facility on the dates and for the purpose indicated below:

Work Order	Date	Description of Service
33-0000	3/95	Warranty repairs
48-0000	3/95	Avionics
33-0001	7/95	Warranty repairs

Stip. ¶ 79.

"GAAS's" Retrofit of "Elevated Aviation's" Aircraft Bearing Serial Number 009

34. Between February 8, 1995 and July 31, 1995 "GAAS" performed an engine retrofit and various other services on "Elevated Aviation's" Falcon 20 aircraft bearing serial number 161 at its "Someplace", Illinois facility. Stip. ¶ 81.

35. Upon completion of the retrofit work, "GAAS" personnel, pursuant to an agreement between "GAAS" and "Elevated Aviation", flew the aircraft to a location outside the State of Illinois at which location "Elevated Aviation" took custody and control of the aircraft from "GAAS". No "Elevated Aviation" employees or representatives were present on the flight. Stip. ¶ 84.

36. "Elevated Aviation's" aircraft returned to "GAAS's" "Someplace", Illinois facility on the dates and for the purposes indicated below:

Work Order	Date	Description of Service
33-0000	10/95	Warranty repairs
33-0001	10/95	Warranty repair

Stip. ¶ 85.

"GAAS's" Retrofit of "Ichabod Crane's" Aircraft Bearing Serial Number 010

37. Between May 16, 1995 and September 23, 1995 "GAAS" performed an engine retrofit and various other services on "Ichabod Crane's" Falcon 20 aircraft bearing serial number 010 at its "Someplace", Illinois facility. Stip. ¶ 87.

38. Upon completion of the retrofit work, "GAAS" personnel, pursuant to an agreement between "GAAS" and "Ichabod Crane", flew "Ichabod Crane's"

aircraft to a location outside the State of Illinois at which location "Ichabod Crane" took custody and control of the aircraft from "GAAS". No "Ichabod Crane" employees or representatives were present on the flight. Stip. ¶ 90.

39. "Ichabod Crane's" aircraft returned to "Someplace", Illinois on the dates and for the purposes indicated below:

RPA	Date	Description of Service
0001	4/96	Warranty repairs
0002	5/96	Warranty repairs
0003	5/96	Warranty repairs

Stip. ¶ 91.

"GAAS's" Retrofit of "American Signcraft" Aircraft Bearing Serial Number 011

40. Between April 23, 1994 and April 6, 1995 "GAAS" performed an engine retrofit and various other services on "American Signcraft's" Falcon 20 aircraft bearing serial number 011 at its "Someplace", Illinois facility. Stip. ¶ 93.

41. Upon completion of the retrofit work, "American Signcraft's" Falcon 20 aircraft was delivered to "Stratosphere Aviation" in Illinois and appropriate SOT was collected and remitted as noted by the Department in its audit report. Stip. ¶ 94. The parties agree, however, that an additional thirty-nine dollars and eighty-nine cents ($39.89) of use tax is due with respect to that transaction. *Id*.

Facts Regarding "GAAS's" Maintenance Service Plan Work, And Its Maintenance/Repair Work On "American Signcraft's" Loaner/Rental Engines, in Illinois

42. On or about June 30, 1994 "American Signcraft" and "GAAS's" then owner, "CAS", entered into an Operating Agreement. Stip. ¶ 99; Stip Ex. 80 (copy of Operating Agreement).

43. Pursuant to ¶ 1 of the Operating Agreement, "GAAS" was appointed by "American Signcraft" as its "Exclusive "American Signcraft" Factory-Sponsored Service and Support Center." Stip. ¶ 100; Stip. Ex. 80, ¶ 1.

44. Paragraph 5 of the Operating Agreement is titled, "Inventory Consignment", and describes, *inter alia*, "American Signcraft's" consignment sales of engine parts to "GAAS". Stip. Ex. 80, pp. 6-7 ¶ 5. That paragraph provides, in pertinent part:

> 5. Inventory Consignment
>
> (a) Seller ["American Signcraft"] shall supply to Buyer ["GAAS"] on consignment at the Hangar Facilities and at other ["GAAS"] facilities a level of engine parts inventory (consisting of new spares, repairs and exchanges) which is determined from time to time by mutual agreement of ["GAAS"] and ["American Signcraft"] on the basis of expected customer demand consistent with past practice. ***
>
> (b) **["GAAS"] shall be invoiced for consigned inventory when such inventory has been invoiced to a customer by ["GAAS"].** ["American Signcraft"] shall invoice ["GAAS"] under normal commercial terms (net 30 days). ["GAAS"] **and** ["American Signcraft"] **shall mutually develop and maintain an operating system that will automatically record ["GAAS's"] sales to customers and calculate agreed-upon prices and discounts applicable to ["GAAS's"] purchase of consigned engine parts inventory from Seller**. ["GAAS"] and ["American Signcraft"] shall each be responsible for their own costs incurred in connection with the development and maintenance of such operating system.
>
> ***

Stip. Ex. 80, pp. 6-7 ¶ 5(a)-(b) (emphasis added).

45. Paragraph 6 of the Operating Agreement is titled, "Purchase of Parts, etc.", and it describes, *inter alia*, "GAAS's" obligation to purchase parts from

"American Signcraft". Stip. Ex. 80, pp. 7-8 ¶ 6. That paragraph provides, in pertinent part:

> 6. Purchase of Parts, etc.
>
> (a) Except for repair services which ["GAAS"] is authorized to perform pursuant to this Agreement, ["GAAS"] shall obtain all of its requirements for new and repaired "American Signcraft" engine parts and repair services directly from ["American Signcraft"], or from third party vendors authorized by ["American Signcraft"]. … Annex A attached hereto describes the discount prices applicable to Policy-Based Parts and Non-Policy Based Parts (as described therein) obtained by ["GAAS"] on consignment from ["American Signcraft"] as provided in Section 5 above (it being understood that the discounts applicable to General Products[*] purchased from ["American Signcraft"] shall be subject to the provisions of Section 6(b) below.
>
> ***

Stip. Ex. 80, pp. 7-8 ¶ 6(a) (* "General Products" defined in ¶ 6(b) as "American Signcraft" non-engine parts").

46. Annex A of the Operating Agreement describes "GAAS's" cost of the engine parts "GAAS" was required to purchase from "American Signcraft". Stip. Ex. 80, Annex A ("The principles used to determine ["GAAS's"] cost of engine parts purchased from ["American Signcraft"] on consignment are described below. In general, the cost to ["GAAS"] to purchase a part from ["American Signcraft"] is based on the type of category of customer that purchases such part from ["GAAS"].").

47. Pursuant to ¶ 7 of the Operating Agreement, "GAAS" agreed to perform services for "American Signcraft's" eligible customers covered under the provisions of "American Signcraft's" "Maintenance Service Plans" ("MSP's"). Stip. ¶ 101; Stip. Ex. 80, p. 8 ¶ 7.

48. "American Signcraft" supplied "GAAS" with the parts necessary to perform the MSP's. Stip. ¶ 102; Stip. Ex. 80, p. 6 ¶ 5(a) & Annex B thereto. That is to say, "GAAS" purchased, from "American Signcraft", the parts that "GAAS" used when performing MSP work. Stip. Ex. 80, Annex B.

49. "American Signcraft" reimbursed "GAAS" for performing services for eligible MSP customers. Stip. Ex. 80, p. 8 ¶ 7 & Annex B.

50. Annex B of the Operating Agreement describes the way "American Signcraft" would calculate the amount it would reimburse "GAAS" for the services "GAAS" performed pursuant to ¶ 7 of the agreement. Stip. Ex. 80, Annex B.

51. "American Signcraft" calculated the amount of "GAAS's" reimbursement using several variables, including the "Actual List Price" of the work "GAAS" performed. Stip. ¶¶ 103-105; Stip. Ex. 80, Annex B (defining "Actual List Price" and other variables). "American Signcraft" calculated the Actual List Price of the work "GAAS" performed using standard labor allowances and rates, and the list price "GAAS" paid for the parts it purchased and used to complete such services. Stip. ¶ 105; Stip. Ex. 80, Annex B ¶ 1. That is, "American Signcraft" reimbursed "GAAS" based, in part, on "GAAS's" labor costs and on "GAAS"' cost for the parts it purchased and used to complete the work. Stip. Ex. 80, Annex B.

52. "GAAS" submitted claims to "American Signcraft" to receive reimbursement for the MSP services it performed. Stip. ¶ 106.

53. Pursuant to paragraph 11 of the Operating Agreement, "American Signcraft" provided loaner/rental engines to "GAAS" for temporary use by customers whose aircraft engines were being serviced. Stip. ¶ 107; Stip. Ex. 80, p. 11 ¶ 11(a).

54. Pursuant to that same paragraph, "GAAS" agreed to perform maintenance and repair services on "American Signcraft's" loaner/rental engines, using parts that "American Signcraft" sold to "GAAS". Stip. ¶ 108; Stip. Ex. 80, pp. 6-7 ¶ 5, p. 12 ¶ 11(b)(iii) & Annex B.

55. "American Signcraft" reimbursed "GAAS" for its maintenance/repair work on "American Signcraft's" loaner/rental engines using the same formula "American Signcraft" used to reimburse "GAAS" for its MSP work. Stip. ¶ 109. "GAAS" similarly submitted claims to "American Signcraft" to obtain reimbursement for its maintenance/repair work on "American Signcraft"'s loaner/rental engines. Stip. ¶ 110.

56. Pursuant to the Operating Agreement, "GAAS" was an independent contractor, and not "American Signcraft's" agent. Stip. Ex. 80, p. 20 ¶ 18(d).

57. After the audit period at issue, "American Signcraft" gave to "GAAS" a "Uniform Sales & Use Tax Certificate Multi-jurisdiction" representing to "GAAS" that "American Signcraft's" transactions with "GAAS" (i.e., "GAAS's" performance of MSP work and maintenance/repairs of "American Signcraft's" loaner/rental engines) were not subject to tax. Stip. ¶ 111.[2]

58. The exemption certificate provided on its face that:

- "American Signcraft" was purchasing "spare parts …" from "GAAS". Stip. Ex. 87.

[2] "GAAS's" MSP work, where it purchased engine and other parts to use when performing warranty work and/or for repairs for purchasers of "American Signcraft's" maintenance service plans (Stip. Ex. 80, pp. 6-7 ¶ 5(a)-(b)), should not be confused with its retrofit work, where "GAAS" did not purchase engines from "American Signcraft". Stip. Ex. 82, p. 6.

- it pertained to transactions undertaken *after* the date it was signed. Stip. Ex. 87 ("This certificate shall be part of each order which we may hereafter give to you, unless otherwise specified, and shall be valid until canceled by us in writing or revoked by the city or state.").
- the reason for the exemption was that ""American Signcraft" was directly paying the tax." Stip. Ex. 87.

Facts Regarding Taxpayer's Acquisition of "GAAS"

59. In May 1994, "American Signcraft" sold "GAAS" to "Creative Aviation Services, LP". In May 1996, "CAS" sold "GAAS" to "CAS/UNC Acquisition Co." and changed its corporate name to "Stratosphere Aviation, Inc." In September 1997, "GAAS" was acquired by the "GenCo". Stip. ¶¶ 13-16; Stip. Ex. 82 (Auditor's Comments), p. 2; Taxpayer's Brief, p. 2 n.1.

60. On or about May 26, 1994, "American Signcraft" and "ABC Aviation Services, Inc.", ("ABC") entered into an "Asset and Stock Purchase Agreement" ("Acquisition Agreement"). Stip. ¶ 95; Stip. Ex. 79 (copy of Acquisition Agreement).

61. On or about June 30, 1994, "ABC" assigned all of its rights and obligations under the Acquisition Agreement to "CAS". Stip. ¶ 96.

62. Pursuant to the Acquisition Agreement, "CAS" acquired substantially all of "American Signcraft's" right, title and interest in certain Hangar Businesses including those located at the "Someplace", Illinois facility. Stip. ¶ 97.

63. After May 26, 1994, "American Signcraft" continued to be engaged in the manufacture, support and distribution of various aviation products and accessories

and providing pre-paid maintenance services for customers relative to the same. Stip. ¶ 98.

Miscellaneous Matters

64. This contested case involves the same issue that was presented in a contested case previously held by the Department's Office of Administrative Hearings, and "Stratosphere Aviation, Inc." is the current owner of the taxpayer in that matter. Pre-Hearing Order, dated 12/10/01, ¶ 3; *see also* Stip. Ex. 81, pp. 1-2; ["SAI's"] Motion to Continue Hearing, dated 4/5/02, ¶ 3.

65. At the time of the pre-hearing conference in this matter, the parties knew that the prior matter would soon be the subject of a recommended decision by the same administrative law judge handling this contested case, and the parties "asked that the hearing date in this matter be set so that they ha[d] an opportunity to review, to the extent possible, the decision in that prior matter." [Pre-Hearing] Order, dated 12/10/01, ¶ 3.

66. The parties had an opportunity to review the agency's decision in that prior matter (which is now on administrative review in the Circuit Court of Cook County, Illinois) before they submitted the stipulated record in this case. *See* ["SAI's"] Motion to Continue Hearing, dated 4/5/02, ¶ 3.

67. "SAI" filed a motion to continue the first hearing date set in this matter, which motion provided, in part:

> Another matter has been proceeding before the Office of Administrative Hearings which may have significant impact on the final stipulation and hearing in this case. As such, the parties were anticipating receiving the Notice of Disposition in the case of the *Department of Revenue v. Allied Signal, Inc.*, Case No. 99-ST-0201.

> Taxpayer received the Notice of Disposition during the week of April 1, 2002 and Taxpayer has not had an opportunity to analyze the disposition and determine its impact on the instant matter. For this reason, Taxpayer seeks a continuance of the hearing as the Notice of Disposition may affect facts which will be incorporated into the Stipulation and the issues which will be addressed at the hearing of this cause.

["SAI's"] Motion to Continue Hearing, dated 4/5/02, ¶ 3; *see also* Department of Revenue v. Allied Signal, Inc., No. 99-ST-0201 (hereinafter "Allied Signal, Inc., No. 99-ST-0201, p. [ ]").

68. "SAI's" motion to continue was granted by an order dated 4/11/02.

Conclusions of Law:

The Illinois General Assembly incorporated into the SOTA several statutory provisions that are also included within the Retailers' Occupation Tax Act ("ROTA"). 35 **ILCS** 115/12. One of the incorporated sections is § 4 of the ROTA, which provides, in pertinent part:

> As soon as practicable after any return is filed, the Department shall examine such return and shall, if necessary, correct such return according to its best judgment and information. … In the event that the return is corrected for any reason other than a mathematical error, any return so corrected by the Department shall be prima facie correct and shall be prima facie evidence of the correctness of the amount of tax due, as shown therein. ***

35 **ILCS** 120/4.

At hearing, the Department introduced a copy of the NTL it issued to "SAI", and the correction of taxpayer's returns, into evidence. Stip. Ex. 1. Pursuant to § 12 of the SOTA, those documents constitute prima facie proof of the correctness of the amount of tax due. 35 **ILCS** 115/12; 35 **ILCS** 120/4. The Department's prima facie case is a

rebuttable presumption. Copilevitz v. Department of Revenue, 41 Ill. 2d 154, 157, 242 N.E.2d 205, 207 (1968); DuPage Liquor Store, Inc. v. McKibbin, 383 Ill. 276, 279, 48 N.E.2d 926, 927 (1943). A taxpayer cannot overcome the presumption merely by denying the accuracy of the Department's assessment. Mel-Park Drugs, Inc. v. Department of Revenue, 218 Ill. App. 3d 203, 217, 577 N.E.2d 1278, 1287 (1st Dist. 1991). Instead, a taxpayer has the burden to present evidence that is consistent, probable and closely identified with its books and records, to show that the assessment is not correct. Fillichio v. Department of Revenue, 15 Ill. 2d 327, 333, 155 N.E.2d 3, 7 (1958); A.R. Barnes & Co. v. Department of Revenue, 173 Ill. App. 3d 826, 833-34, 527 N.E.2d 1048, 1053 (1st Dist. 1988).

Issue 1: Are "GAAS's" Retrofits Subject to SOT

"GAAS" has identified this first issue as "whether … [it] is subject to [SOT] on property transferred incident to its sale of engine retrofit and refurbishment services, when the property transferred was physically delivered to the customer outside Illinois[.]" Taxpayer's Brief, p. 1. Section 3-45 of the SOTA provides:

> Interstate commerce exemption. No tax is imposed under this Act upon the privilege of engaging in a business in interstate commerce or otherwise when the business may not, under the Constitution and statutes of the United States, be made the subject of taxation by this State.

35 **ILCS** 115/3-45.

The Department has promulgated a regulation interpreting § 3-45 of the SOTA. The first two paragraphs of Illinois SOT regulation § 140.501 provide:

> Sales of Service Involving Property Originating in Illinois
> a) Where tangible personal property is located in this State at the time of its transfer (or is subsequently produced in Illinois) as an incident to a sale of service, and is then

> delivered in Illinois, the serviceman incurs Service Occupation Tax liability on the selling price of the property. The sale is not deemed to be in interstate commerce if the purchaser or his representative receives the physical possession of such property in this State. This is so notwithstanding the fact that the purchaser may, after receiving physical possession of the property in this State, transport or send the property out of the State for use outside the State or for use in the conduct of interstate commerce. The place at which the contract of sale of the service or contract to sell the service is negotiated and executed and the place at which title to the property passes to the purchaser are immaterial. The place at which the purchaser resides is also immaterial. Except as is set out at Section 140.501(d) of this Part, it also makes no difference that the purchaser is a carrier when that happens to be the case.
>
> b) The serviceman does not incur Service Occupation Tax liability on property which he resells as an incident to a sale of service under an agreement by which the serviceman is obligated to make physical delivery of the goods from a point in this State to a point outside this State, not to be returned to a point within this State, provided that such delivery is actually made. Nor does the tax apply to property which the serviceman resells as an incident to a sale of service under an agreement by which the serviceman, by carrier (when the carrier is not also the purchaser) or by mail, delivers the property from a point in this State to a point outside this State, not to be returned to a point within this State. The place at which title to the property passes to the purchaser is immaterial. The place at which the contract of sale of the service or contract to sell the service is negotiated and executed and the place at which the purchaser resides are also immaterial. Sales of service of the type described in this paragraph are deemed to be within the protection of the Commerce Clause of the Constitution of the United States.
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> * * *

86 Ill. Admin. Code § 140.501; 14 Ill. Reg. 262 (eff. January 1, 1990).

The Parties' Stipulation Regarding "GAAS's" Redelivery Of Its Customer's Aircraft After Its Retrofits Were Completed Is Not Probative Of The Issue In Dispute

As the second paragraph of the applicable regulation shows, the resolution of this first issue requires a determination whether "GAAS" delivered physical possession of the goods it resold and installed into others' aircraft, as an incident to its sales of service, to its customers in Illinois. The Department argues that it did (Department's Brief, p. 4), "GAAS" claims it did not. Taxpayer's Brief, p. 15. After considering all of the evidence submitted by the parties, and the facts to which they stipulated, the succinct answer to that question is, "I don't know." That is to say, no documentary evidence in this record, and no stipulated facts, establish that "GAAS" delivered the goods it transferred incident to its sales of service to its customers in Illinois. Similarly, no documentary evidence, and no stipulations of fact, specifically establish that the goods "GAAS" transferred to its customers — as opposed to the aircraft, which "GAAS" did *not* transfer — were, in fact, resold "under an agreement by which ["GAAS"] was obligated to make physical delivery of those goods from a point in this State to a point outside this State, not to be returned to a point within this State." 86 Ill. Admin. Code § 140.501(b).

As I have already indicated, the Department's prima facie case is a rebuttable presumption. The statutory presumption extends to all elements necessary for a determination that tax is due as determined by the Department. *E.g.* Branson v. Department of Revenue, 68 Ill. 2d 247, 258, 659 N.E.2d 961, 966-67 (1995) ("nothing more [than the certified copy of the NPL] is needed to prove the Department's claim for a tax penalty against the corporate officer or employee."). That is to say, the presumption extends to the agency's determination that "GAAS" is engaged in a service occupation (Soho Club, Inc. v. Department of Revenue, 269 Ill. App. 3d 220, 232, 645 N.E.2d 1060, 1068 (1st Dist. 1995)), and that the transactions at issue here were subject to SOT. 35

ILCS 115/12 (incorporating, *inter alia*, §§ 4 and 7 of the ROTA). Further, this matter involves an exemption from taxation, and "GAAS" bears the burden to show that its agreement required it to deliver the goods it transferred incident to its sales of service from a point within Illinois to a point outside Illinois. 86 Ill. Admin. Code § 140.501(b); *see also* Du-Mont Ventilating Co. v. Department of Revenue, 73 Ill. 2d 243, 249, 383 N.E.2d 197, 201 (1978) (taxpayer satisfied its burden to prove that property used fit the exemption claimed).

In this case, "GAAS", as its prior owner did in the prior contested case, has sought to prove that it delivered the goods it transferred incident to its sales of service by reference to its undisputed redeliveries of its customers' aircraft outside Illinois. Taxpayer's Brief, p. 15. "GAAS" transfers many different types of goods incident to its sales of service, but it did not transfer its customer's aircraft to the customer. 35 **ILCS** 115/2 (definition of "transfer"). "GAAS" is a bailee of its customer's aircraft, just as any person engaged in the business of repairing or servicing other people's property is a bailee of the property they service. Clark v. Fields, 37 Ill. 2d 583, 229 N.E.2d 676 (1967) (person who took possession of another's aircraft to repair it was a bailee); Fuller's Car Wash, Inc. v. Liberty Mutual Insurance Co., 298 Ill. App. 3d 167, 174, 698 N.E.2d 237, 242-43 (2nd Dist. 1998) (customer's delivery of car to employee of full-service car wash created bailment); *see also*, 8A Am. Jur. 2d *Aviation* § 38 (Bailment or Lease of Airplane) (1997) ("The delivery of an airplane to a mechanic for the purpose of repairs also creates the relation of bailor and bailee …."); 8A Am. Jur. 2d Bailments § 9 (Lucrative Bailments, Bailments for Mutual Benefit) (1997) ("A mutual benefit bailment

is created when a chattel is delivered by its owner to another for repairs, service, or alteration.").

Since "GAAS" does not transfer customers' aircraft, but only performs services on them, it has not carried its burden by citing to the Department's stipulations that "GAAS" redelivered possession of its customer's aircraft by flying them back to their respective owners, after its retrofit work was completed. Stip. ¶¶ 26, 32, 35, 42, 45, 48, 51, 56, 59, 61, 64, 67, 70, 75, 78, 81, 84, 87, 90, 93, 94. "GAAS", for example, cites to the stipulations for the proposition that it "was obligated by its customer agreement to physically deliver … the engine retrofits and aircraft refurbishments in question to the aircraft owners at points outside Illinois." Taxpayer's Brief, p. 15. What the stipulations actually say, however, is that, upon completion of the retrofit work, its personnel, pursuant to an agreement between "GAAS" and the customer, flew a customer's aircraft to the customer at a point outside Illinois, where the customer took custody and control of the aircraft. Stip. ¶¶ 26, 32, 35, 42, 45, 48, 51, 56, 59, 61, 64, 67, 70, 75, 78, 81, 84, 87, 90. But whether the agreement pursuant to which "GAAS" redelivered the customer's aircraft was the agreement pursuant to which it agreed to perform retrofit services in the first place is never addressed by the stipulations.

My conclusion here is not that a serviceman's redelivery of its customer/bailor's aircraft (or other vehicle) into which the serviceman transfers goods by installing them therein, can *never* be the means by which the serviceman agrees to deliver the goods that he transfers as an incident to his sale of service. Whether the agreement does or does not, however, must be determined by reviewing the terms of the service agreement itself. *See* Exhibits, Inc. v. Sweet, 303 Ill. App. 3d 423, 709 N.E.2d 236 (1st Dist. 1998). "GAAS"

bears the burden to show that its transfers were not taxable (35 **ILCS** 120/7; 35 **ILCS** 115/12), and it has not satisfied that burden because of the dearth of facts included in this stipulated record concerning the relevant terms of "GAAS's" retrofit agreements during the period at issue.

That conclusion is also based on my knowledge of the express terms of the written contracts "GAAS" used prior to this audit period. *See* Stip. ¶¶ 95-99; Stip. Ex. 79-82; Pre-Hearing Order; "SAI's" Motion to Continue Hearing (asking to continue the hearing date in this matter until it had time to review the agency decision issued in the contested case involving the same issue and the same business, albeit when "GAAS" was owned by "American Signcraft"). This record does not include any facts or evidence showing that "GAAS" changed its prior business practice of using written contracts to document the terms of its retrofit agreements with customers during the period at issue. Both parties are also well aware of the facts regarding the way "GAAS" conducted business previously, when "American Signcraft" owned it. Indeed, taxpayer asked to defer its submission of a stipulated record in this case until the agency issued its decision in that prior contested case. Further, both parties cited that prior case to support their positions here,[3] and both know that that prior contested case involved "GAAS's" business, when "GAAS" was owned by a different person. Stip. ¶¶ 95-99; Stip. Ex. 79-82; Pre-Hearing Order; "SAI's" Motion to Continue Hearing.

Rather than submitting copies of the written agreements between "GAAS" and its retrofit customers when "CAS" owned "GAAS", the parties stipulated to facts identifying only one particular agreement that was to occur *after* a retrofit was completed.

Specifically, and with only slight variations, the parties entered into the following stipulations for each retrofit that "GAAS" performed in Illinois:

> Between … [aircraft arrival date] and … [aircraft departure date] "CAS" performed an engine retrofit on [customer's] Falcon 20 aircraft … at its "Someplace", Illinois hangar facility.
>
> ***
>
> Upon completion of the retrofit work … "CAS" personnel, pursuant to an agreement between "CAS" and [customer], … flew [customer's] Falcon 20 aircraft … to a location outside the State of Illinois at which location [customer] took custody and control of the aircraft from "CAS". No [customer] employees or representatives were present on the flight.

Stip. ¶¶ 26, 32 (retrofit 1, aircraft serial no. XXX), 35, 42 (retrofit 2, aircraft serial no. XXX), 45, 48 (retrofit 3, aircraft serial no. XXX), 51, 54 (retrofit 4, aircraft serial no. XXX), 56, 59 (retrofit 5, aircraft serial no. XXX), 61, 64 (retrofit 6, aircraft serial no. XXX), 67, 70 (retrofit 7, aircraft serial no. XXX), 75, 78 (retrofit 8, aircraft serial no. XXX), 81, 84 (retrofit 9, aircraft serial no. XXX), 87, 90 (retrofit 10, aircraft serial no. XXX), 93, 94 (retrofit 11, aircraft serial no. XXX).

The question left unanswered by the parties' stipulations is whether "GAAS's" retrofit agreements required it to deliver possession of the goods it transfers as an incident thereto to the customer outside Illinois. 86 Ill. Admin. Code § 140.501(b). In its briefs, "GAAS" implies that it is. That is, it argues that, "[t]he facts here are that once the Taxpayer finishes its retrofit or refurbishment work, the taxpayer is obligated *under its customer agreement* to physically deliver the aircraft — with the new engines or refinished parts — to the service customer, the aircraft owner, at an out-of-state location,

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[3] Counsel for "GAAS" cited that prior agency decision both to criticize the conclusions of law reached therein, and to distinguish the facts found in that case from the facts to which the

and that the Taxpayer discharged this obligation in each of the ten transactions at issue." Taxpayer's Brief, p. 5 (emphasis added); *id*. p. 15. "GAAS's" use of the singular ("under its customer agreement") suggests that its agreement to redeliver possession of an aircraft to a customer was the only agreement in effect between it and its customer. But that is not what the parties' stipulations of fact actually say (Stip. ¶¶ 32, 42, 48, 54, 59, 64, 70, 78, 84, 90, 94), and that is not the way "GAAS" conducted business before "CAS" owned it.

Previously, "GAAS" entered into written agreements for every retrofit, which agreements referred to those retrofits as "modifications." Department of Revenue v. "American Signcraft", Inc., p. 3 (finding of fact 4). In each of those modification agreements, "GAAS" notified its customer that it was willing to consider redelivering possession of a customer's aircraft to the customer, after the modification was completed, by flying it back to the customer. *Id*. pp. 7, 9, 12, 14, 16, 18, 20, 22-23, 25, 27, 28-29 (respectively, finding of fact numbers 17, 24, 31, 37, 43, 50, 57, 63, 70, 76, 83, 90). The terms of those modification agreements, however, expressly conditioned "GAAS's" agreement to redeliver a customer's aircraft outside Illinois upon the customer's first coming into Illinois, inspecting and then taking delivery of the modification *inside Illinois*. *Id*. pp. 7, 9, 12, 14, 16, 18, 20, 22-23, 25, 27, 28-29 (respectively, finding of fact numbers 17, 24, 31, 37, 43, 50, 57, 63, 70, 76, 83, 90). In short, "GAAS's" own written modification agreements — the agreements pursuant to which it transferred property as an incident to its sales of service — required that the modification be delivered to a

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parties stipulated here. Taxpayer's Brief, pp. 11-14; Taxpayer's Reply, p. 4.

customer in Illinois, whereas the aircraft itself could, thereafter, be redelivered to the customer outside Illinois.

My recitation of the express terms of "GAAS's" modification contracts during a prior audit period is intended to do two things: (1) explain why "GAAS's" stipulated agreement to redeliver a customer's aircraft to the customer outside Illinois need not be considered "GAAS's" delivery of the goods it transferred to the customer pursuant to the agreement for "GAAS's" sales of service; and (2) detail how the record in this case fails to articulate whether "GAAS's" agreement to redeliver its customer's aircraft during this audit period was required by the agreement pursuant to which "GAAS" agreed to provide retrofit services.

In its reply, "GAAS" points out that the facts to which the parties stipulated here are not the same as the facts found in the previous contested case involving "GAAS" when "CAS" did not own it. Taxpayer's Reply, p. 4. Without a doubt, that is true. "GAAS's" argument, however, suggests that the taxpayer in that prior administrative case is a stranger to this dispute. The record in this matter proves otherwise. Stip. ¶¶ 95-99; Stip. Ex. 79-82; Pre-Hearing Order; "SAI's" Motion to Continue. Regardless which corporate entity owned it, "GAAS" was, during the prior audit period and during the period at issue here, an FAA-certified repair station doing business in "Someplace", Illinois. Stip. Ex. 84. At all times, it performed retrofits of others aircraft. *See id*.

Nor does "GAAS's" argument about the stipulated record in this case say anything about whether the condition precedent incorporated into "GAAS's" prior written retrofit agreements was included within the retrofit agreements it used during the period at issue. Were "GAAS's customers required to come into Illinois and accept

"GAAS's" retrofit services — and the goods installed into the aircraft, pursuant thereto — as a condition of "GAAS's" willingness to redeliver possession of the aircraft to the customer outside Illinois? About this pertinent question, the record is silent. Here, the evidence "GAAS" relies on is proof that it returned customers' aircraft to customers outside Illinois, but the evidence that is probative of the fact at issue is evidence that would show where "GAAS's" agreements required it to deliver the goods it installed into the customer's aircraft. 86 Ill. Admin. Code § 140.501(a)-(b).

I acknowledge that "GAAS" could have changed its business practices after "CAS" acquired it. That is to say, during the audit period at issue, "GAAS" could have changed the provisions of the written agreements it used before. "GAAS", for example, made a significant change in the way it did business, after "American Signcraft" sold it to "CAS". When "GAAS" was owned by "American Signcraft", "GAAS" purchased engines from the manufacturer, a related corporation, and thereafter transferred possession of and title to those engines to its customers as part of its retrofits. Here, "GAAS" did *not* transfer the engines to its customers, either in Illinois or anywhere else, because the customer purchased those engines directly from the manufacturer, "American Signcraft". Stip. Ex. 81, pp. 2-3; Stip. Ex. 82, pp. 5-6. "GAAS" billed each customer for the services required to install those engines, but not for the cost price of those new engines. *See supra*, p. 4 (finding of fact no. 9); Stip. Ex. 81, pp. 2-3; Stip. Ex. 82, pp. 5-6. Thus, in this case, the Department did not measure SOT by "GAAS's" cost price of the engines it installed during a retrofit, because "GAAS" never purchased or transferred those engines to its customers. *See* Stip. Ex. 86.

At least for purposes of this first issue, however, that was the only significant change that this record shows that "GAAS" made in the way it conducted business from when "American Signcraft" owned it to when "CAS" owned it. Stip. Ex. 81, pp. 2-3; Stip. Ex. 82, pp. 5-6. Further, the parties' stipulations do not provide that, once "CAS" acquired "GAAS", it ceased using written agreements to document the express terms of "GAAS's" agreements to perform retrofit and refurbishment services for customers. That would indeed be an unlikely event, since customers paid "CAS" several hundred thousand dollars to over one million dollars for "GAAS's" retrofit services and the materials transferred incident thereto. Stip. Ex. 86 (copy of auditor's calculations of tax based on invoice totals). Considering that, after it was acquired by "CAS", "GAAS" continued to use a writing to document its out-of-state deliveries of aircraft to customers (Stip. Ex. 82, p. 5), it is only logical to conclude that "GAAS" also continued to use written contracts to document the terms of its agreements to perform retrofits for customers. "GAAS" either has the written agreements pursuant to which it transferred goods incident to its sales of services for each of the retrofits, or it had the ability to establish that it did not use written retrofit or modification agreements.

To sum up then, the facts and evidence admitted by stipulation are inconclusive to show where "GAAS's" agreements called for it to deliver the goods it transferred incident to its sales of service. This first issue is decided in the Department's favor because §§ 4 and 7 of the ROTA, incorporated into the SOTA, provide that the Department's determinations are prima facie correct and that the burden of proving that transactions are not taxable lies on the person on whom tax would otherwise be assessed. 35 **ILCS** 120/4, 7; 35 **ILCS** 115/12. "GAAS" has not carried its burden to establish that

the goods it transferred incident to its sales of service were resold "as an incident to a sale of service under an agreement by which ["GAAS" was] obligated to make physical delivery of the goods from a point in this State to a point outside this State …." 86 Ill. Admin. Code § 140.501(b). I will not imply that "GAAS's" agreements to perform retrofit services required it to deliver the goods it transferred incident to its sales of service to its customers outside Illinois because, in the past, "GAAS's" written retrofit agreements required that its customers take delivery of the retrofit while the aircraft was still inside Illinois. This record does not reflect that "GAAS's" agreements to provide retrofit services, during the applicable period, no longer included that condition precedent. Indeed, this record says nothing whatever about how "GAAS" would tender its retrofit services, or how it would deliver the goods, installed as an incident thereto, to its customers.

The Private Letter Rulings "GAAS" Cites Do Not Set Forth A Statement Of Department Policy

"GAAS" cites to two private letter rulings in which the Department notified others that their transactions would not be subject to SOT or to ROT. Taxpayer's Brief, pp. 5-7. It contends, thereafter, that those private letter rulings constitute a statement of the Department's policy vis-à-vis exempt interstate sales under the SOT, and that its transfers must similarly be considered exempt. *Id*. The letter rulings "GAAS" cites, however, do not constitute generally applicable statements of the Department's policy. Rather, the Department's express statements of what its policy is with regard to transactions that will be treated as exempt from SOT because they are transactions in interstate commerce, is set forth within the applicable SOT regulation, § 140.501.

The singular thing that both PLR 92-0543 and this matter have in common is that in both, there is no articulation of the specific terms of the serviceman's agreements for its sale of services. The specific terms of the agreements the serviceman described in that letter ruling are not detailed therein, and "GAAS", after having the opportunity to review the findings and conclusions in the agency's prior administrative decision involving "GAAS's" business during prior periods, chose not to submit copies of its retrofit agreements as part of the stipulated record in this case. Thus, and despite "GAAS's" argument that the facts here are "virtually identical" to the facts set forth in PLR 92-0543 (Taxpayer's Brief, p. 5), I have no idea whether the agreements the taxpayer used in that case have the same provisions that "GAAS's" agreements had during the period at issue.

I certainly know that "GAAS's" business is very different than the businesses described in the two private letter rulings, and in its hypothetical watch repair business. *See* Taxpayer's Brief, p. 15. The prior agency decision in "American Signcraft", Inc., No. 99-ST-0201, concluded, *inter alia*, that "GAAS" delivered the goods it transferred to a customer incident to its sale of service, once it made them fully functioning component parts of its customer's aircraft. "American Signcraft", Inc., No. 99-ST-0201, p. 52. That conclusion was based on the specific nature of "GAAS's" business, and based on the overriding federal regulatory scheme applicable to persons engaged in "GAAS's" business. "American Signcraft", Inc., No. 99-ST-0201, pp. 46-52. When an FAA certified inspector approves a major alteration or repair of an aircraft or a component part thereof, that act has independent legal significance. As a matter of federal law, that approval acts as the inspector's certification that the aircraft or component part is airworthy. Until that point, the aircraft could not, legally, be flown anywhere. *Id*. p. 48

(*citing* 14 C.F.R. § 43.5). That overriding federal regulatory scheme applies to the same business "GAAS" conducted during the years at issue, when "CAS" owned it. *See* Stip. Ex. 84. I trust that "GAAS" does not really believe that persons engaged in the business of customizing buses, selling coal, or repairing watches operate in a manner that is "virtually identical" to the way it conducts its business.

One of the reasons why letter rulings have no precedential effect, moreover, is that the process by which a person seeks a private letter ruling is comparatively informal, and the issuing agency relies on the requestor's representations of its conduct, or the terms of its agreements when responding to a request. *See, e.g.*, PLR 00-0018, p. 2 (restating requestor's description of its agreements, rather than detailing what the express terms of the agreements were). Further, the issuing agency often does not perform the same detailed fact-finding and legal analysis when responding to the request, as is required in a contested case. Both letter rulings cited by "GAAS" confirm those facts. PLR 92-0543; PLR 00-0018. Indeed, the policy that *is* clearly set forth in the rulings cited by "GAAS" is reflected by the second letter writer's admonition to the requestor that the Department would not be bound by the ruling if the facts as stated in the request were other than as they were described. PLR 00-0018.

Unlike the comparatively informal process of obtaining a private letter ruling, a contested case hearing is subject to the fundamental rules of Illinois evidence (5 **ILCS** 100/10-40; 35 **ILCS** 115/20a), and corporate taxpayers are ordinarily required to be represented by counsel. 86 Ill. Admin. Code § 200.110(a). In a contested tax hearing, a taxpayer seeking to rebut the prima facie correctness of the Department's determinations must prove its position with documentary evidence closely associated with its books and

records. 35 **ILCS** 120/7; 35 **ILCS** 105/12; A.R. Barnes & Co. v. Department of Revenue, 173 Ill. App. 3d 826, 833-34, 527 N.E.2d 1048, 1053 (1st Dist. 1988). A stipulation can obviate the need for documentary evidence on any particular fact, but the particular facts to which the parties stipulated here do not address the specific fact issue presented by this case, and by SOT regulation § 140.501(b). This record includes no stipulations regarding the existence of any of the express terms of the agreement "GAAS" had with its customers to perform retrofit services — services that required months for "GAAS" to complete, and for which services "GAAS's" customers paid considerable amounts. Stip. ¶¶ 26, 35, 45, 51, 61, 67, 75, 81, 87, 93; Stip. Ex. 86. The parties' stipulations do not completely describe all of the terms of the agreement between the parties to the retrofit. After its review of the agency's decision in the contested case involving "GAAS's" business during prior years, "GAAS's" new owner chose to submit its case for decision on stipulated facts regarding its retrofits, but without the agreements themselves. I must conclude, therefore, that taxpayer chose to exclude documentary evidence probative of the central factual issue.

Finally, it is curious that "GAAS" cites Illinois' Commercial Code when criticizing the agency's conclusion that, during a prior audit period, "GAAS's" delivery of its service work constituted delivery of the aircraft engines and other goods "GAAS" installed into aircraft, as an incident to performing that service work. Taxpayer's Brief, p. 14 (*citing* 810 **ILCS** 5/2-503(1)). "GAAS's" own written modification agreements required its customers to come into Illinois to inspect and take "delivery" of the modifications "GAAS" took months to perform. *See* "American Signcraft", Inc., No. 99-ST-0201, pp. 7, 9, 12, 14, 16, 18, 20, 22-23, 25, 27, 28-29 (respectively, finding of fact

numbers 17, 24, 31, 37, 43, 50, 57, 63, 70, 76, 83, 90). Yet "GAAS" now contends that, despite its own express contractual distinction between delivery of the modification and its subsequent delivery of the aircraft, the Department must not be able to recognize any distinction between the two. Taxpayer's Brief, p. 14.

"GAAS's" criticism, however, is inconsistent with the Illinois Commercial Code's underlying purpose of allowing contracting parties to fashion the specific terms of their agreements, and with the UCC's drafters' intent that the law should attempt to give meaningful effect to the terms to which contracting parties agreed. 810 **ILCS** 5/1-102(3) ("Purposes, rules of construction, variation by agreement"). "GAAS's" contracts specifically identified the manner by which it would tender delivery of its services, and, by implication, the goods it transferred incident to its sales of services. "American Signcraft", Inc., No. 99-ST-0201, pp. 7, 9, 12, 14, 16, 18, 20, 22-23, 25, 27, 28-29 (respectively, finding of fact numbers 17, 24, 31, 37, 43, 50, 57, 63, 70, 76, 83, 90). "GAAS" itself distinguished between the way it would tender delivery of its retrofit services and the way its customer could arrange to retake possession of its aircraft, after the customer took delivery of the retrofit inside Illinois. Thus, it is "GAAS", and "GAAS" alone, that continues to reject the fact that its own written agreements distinguished between its delivery of its retrofits — which occurred in Illinois — and its subsequent delivery of the customer's aircraft — which may or may not have occurred in Illinois. In the prior decision, the agency heeded § 503(1) of Illinois' Commercial Code, by actually reviewing and taking into account the express provisions of the parties' written agreements. "GAAS's" counterintuitive criticism of that approach, in this case, is

exacerbated by its decision to not submit for consideration copies of its agreements to provide retrofit services during the period at issue.

No "Underground Rule" Exists That Precludes "GAAS's" Claim Because It Did Not Know Whether Its Customers Would Fly Aircraft On Which "GAAS" Performed Retrofits Back Into Illinois

"GAAS" claims that the Department assessed tax against it because "GAAS" could not determine, at or about the time it provided retrofit services, whether its customers would return their aircraft to Illinois for any subsequent warranty work. Taxpayer's Brief, pp. 7-10. "GAAS" is actually complaining about statements made in a memo written by an employee in the Department's Technical Support Section to a Department audit supervisor who was assigned to the audit of "GAAS's" prior owner, "American Signcraft". Taxpayer's Brief, pp. 7-8 (quoting the opinion of Terry Charlton, a Department attorney) & n.3; Stip. Ex. 83 (copy of tech support memo in prior case). The audit supervisor in this current dispute referred to that prior technical support advice in the report he wrote regarding this audit. Stip. Ex. 81, pp. 2-3. Without saying so directly, he apparently accepted the advice the prior audit supervisor received from the Department's legal division as being interpretive of how SOT regulation § 140.501 applied to the facts of "GAAS's" retrofit transactions here. *Id*.

While the Department initially argues that the retrofit transactions are subject to SOT because "GAAS" delivered the goods it installed into customers' aircraft to the customers in Illinois (Department's Brief, pp. 2-3), it later argues that "GAAS" failed to rebut the presumptive correctness of the Department's determination that tax was due because "GAAS" could not establish that its customers would not fly the aircraft — and the installed goods — back into Illinois. Department's Brief, pp. 6-8. The Department's

position is based on the text of SOT regulation § 140.501(b), which provides that, "The serviceman does not incur Service Occupation Tax liability on property which he resells as an incident to a sale of service under an agreement by which the serviceman is obligated to make physical delivery of the goods from a point in this State to a point outside this State, *not to be returned to a point within this State*, provided that such delivery is actually made. 86 Ill. Admin. Code § 140.501(b) (emphasis added). Specifically, the Department argues that:

> The Taxpayer is required by statute to collect Service Use Tax absent a claim of an exemption by a customer. No evidence has been produced to prove that any of the Taxpayers' customers made any such claim. In addition, the record is silent with respect to any attempt on the part of the Taxpayer to inquire. Based on the presumption of taxation set out in the statute, the Taxpayer was required to act in light of its own ignorance[,] collect Service Use Tax from its customers and remit Service Occupation Tax to the Department. In accordance with the presumption that all sales of tangible personal property are taxable unless the contrary is established, the Taxpayer, not knowing whether the property [installed into customers' aircraft] would return to Illinois, was required by the statute to assume that it would.

Department's Brief, p. 8.

What the Department asserts, however, engrafts a significant addition to the documentation required to establish proof that a particular sale of service was in interstate commerce. Subparagraph (c) of the interstate commerce regulation describes the type of documentary evidence a serviceman must keep to show that certain transactions were exempt sales of service in interstate commerce. 86 Ill. Admin Code § 140.501(c). That part of the regulation provides:

> c) To establish that the selling price of property sold as an incident to any given sale of service is exempt because

> the property is delivered by the serviceman from a point within this State to a point outside this State under the terms of an agreement with the purchaser, the serviceman will be required to retain in his records, to support deductions taken on his tax returns, proof which satisfies the Department that there was such an agreement and a bona fide delivery, outside this State, of the property involved in the sale of service. The most acceptable proof of this fact will be:
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> 1) If shipped by a common carrier: A waybill or bill of lading requiring delivery outside this State;
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> 2) if sent by mail: An authorized receipt from the United States Post Office Department, for articles sent by registered mail, parcel post, ordinary mail or otherwise, showing the name of the addressee, the point outside Illinois to which the property is mailed and the date of such mailing; if the receipt does not comply with these requirements, other supporting evidence will be required;
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> 3) if sent by the serviceman's own transportation equipment: A trip sheet signed by the person making delivery for the serviceman and showing the name, address and signature of the person to whom the goods were delivered outside this State; or, in lieu thereof, an affidavit signed by the purchaser or his representative, showing the name and address of the serviceman, the name and address of the purchaser and the time and place of such delivery outside Illinois by the serviceman, together with other supporting data as required by Section 140.701(c) of this Part and by Section 11 of the Act.

86 Ill. Admin. Code § 140.501(c).

The Department's position seems to be that, in order to establish that a particular sale of service was exempt as being in interstate commerce, a serviceman must, in addition to complying with the requirements described in SOT regulation § 140.501(c), obtain from its customers a sworn statement that the goods transferred incident to the sale of service would never be brought back into Illinois. Subparagraph (b) of regulation § 140.501 has, since at least 1989, included the proviso that the goods transferred were "not to be returned to a point within this State …." During that time, however, § 140.501(c)

never placed on the serviceman the burden to obtain written proof from a customer that the goods delivered to it outside Illinois would never be brought into Illinois.

Nor does the decision in Exhibits, Inc. v. Sweet require a serviceman to obtain the exemption certificates the Department asserts "GAAS" must have obtained and kept here. Exhibits, Inc. v. Sweet, 303 Ill. App. 3d 423, 709 N.E.2d 236 (1st Dist. 1998). The decision in Exhibits, Inc. stands foursquare for the proposition that, where a contract pursuant to which a serviceman makes a sale of service provides that the goods transferred will be returned to Illinois immediately after their delivery and use outside Illinois, the service agreement is not in interstate commerce. Exhibits, Inc., 303 Ill. App. 3d at 427, 709 N.E.2d at 239 ("The parties stipulated that at the time of the sales Exhibits had arranged for return shipment of the exhibits back to Illinois. Under the facts presented, the Department could impose a tax on the transactions according to the regulation."). The holding in that case was not that, in all cases, a serviceman must document that the goods it delivers outside Illinois will never find their way back into Illinois. Exhibits, Inc., 303 Ill. App. 3d at 435, 709 N.E.2d at 244 ("We conclude that Exhibits has failed to demonstrate that the imposition of the Service Occupation Tax Act *to these transactions* offends the commerce clause") (emphasis added). Although an exemption certificate as suggested by the Department might serve a useful purpose in an interstate commerce dispute, it is not required by law.

"GAAS", moreover, is correct to question the correctness of some of the legal opinions described in a memo written by the Department's Technical Support Section to the audit supervisor regarding the audit of "GAAS's" business when "American

Signcraft" owned it. *See* Stip. Ex. 83.[4] Some of the conclusions described in that memo either ignore or fail to appreciate the distinction "GAAS's" own written agreements made between its Illinois deliveries of the goods installed pursuant to its sales of service (i.e., its retrofits), and its deliveries of its customers' aircraft, after those services were completed. In fact, the notion that "GAAS" somehow waived its claim of exemption when the customer flew the aircraft back into Illinois for warranty work, confirms that Charlton viewed the aircraft — instead of the aircraft engines, etc. — as the goods being transferred by "GAAS", incident to its sale of service. It further confirms that Charlton either never actually read the agreements pursuant to which "GAAS" performed retrofit

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[4] The audit supervisor asked the following question and received the following response:

> [Question] 140.501(b) applies when the delivered goods are delivered to a point outside this State, not to be returned to a point within this State. Any warranty work, additional maintenance work, and eventual aircraft inspections are done at any of the taxpayer's authorized service facilities. Many times, the aircraft is returned to the original facility where the work was done because all of the specifications, schematics, and service work orders are there. Will 140.501(b) still apply if it is unknown whether the aircraft will be returned to Illinois; if the aircraft does in fact return to Illinois for service work; or, if the aircraft uses or may use any Illinois airport facility?
>
> Is a signed and notarized "Aircraft Final Acceptance and Delivery" form (see attached copy) adequate to satisfy the requirement of 140.501(c)?
>
> [Answer] 140.501(b) will apply even if it is unknown at the time the work is completed whether the aircraft will be returned to Illinois. However, according to Terry Charlton, if during the audit period, the aircraft does in fact return to Illinois for service work (after the aircraft has been delivered, or the aircraft uses an Illinois airport facility after the aircraft has been delivered), we can then pick up tax on the original service work because the interstate commerce exemption would not apply (the aircraft was returned to Illinois and thus negates the exemption available under 140.501(b)). If the time when the aircraft returns to Illinois is outside the audit period, we are on shaky ground and probably should not pick up tax on the service work.
>
> A signed and notarized "Aircraft Delivery Acceptance and Delivery" form is not conclusive, but it is good evidence that the requirement of 140.501(c) has been met.

or modification services, or that he failed to appreciate that, under those express terms of those agreements, "GAAS" demanded that it deliver the goods it transferred to the customer in Illinois as a condition precedent of its willingness to redeliver the aircraft outside Illinois. Once "GAAS" delivered the goods it actually transferred incident to its sales of services, in Illinois, it didn't really matter where "GAAS" arranged to deliver the aircraft itself. 86 Ill. Admin. Code § 140.501(a)-(b).

Further, there is nothing within the text of SOT regulation § 140.501 that provides any basis for concluding that a serviceman has somehow "waived" its ability to claim an interstate commerce exemption where that waiver is based on its customers' acts, not on the serviceman's acts. Nor is there any basis for concluding that the applicable regulation provides some time limitation, e.g., during an audit period, during which the Department may treat a serviceman's customer's independent act as a waiver of an exemption that is expressly extended to the serviceman itself. 86 Ill. Admin. Code § 140.501.

In sum, I agree with "GAAS's" challenges to the Department's specific argument, quoted *supra*, at p. 36. My conclusion that "GAAS's" retrofits are not transfers in interstate commerce, however, is not based on the fact that its customers flew their aircraft back into Illinois after "GAAS" performed the retrofits, nor is it based on the fact that "GAAS" did not obtain and keep exemption certificates regarding the transactions at issue. Rather, "GAAS" has failed to rebut the Department's determination that the transactions were subject to tax because it has failed to establish that its agreements to provide retrofit services required it to deliver the goods it transferred incident to its sales of services to customers outside Illinois. 35 **ILCS** 120/7; 35 **ILCS** 115/12; 86 Ill. Admin. Code § 140.501(b).

Stip. Ex. 83, p. 2.

"GAAS's" Constitutional Objections

"GAAS" argues that what it calls the Department's "unwritten" or "underground" rule (*see supra*) is unconstitutional because it subjects it to impermissible multiple taxation (Taxpayer's Brief, p. 17), and because it places greater burdens on interstate commerce than on intrastate commerce (*id*., pp. 18-20). "GAAS's" constitutional objections are inapplicable here, however, because the "unwritten rule" it complains of does not form the factual bases for my conclusion that it is subject to SOT regarding the transactions at issue. I expressly reject the notion that "GAAS" has "waived" its ability to claim the interstate commerce exemption because its customers flew aircraft "GAAS" previously retrofitted back into Illinois. Nor do I conclude that "GAAS" failed to rebut the Department's prima facie case because it did not submit into evidence exemption certificates from its retrofit customers to the effect that they would never bring their retrofitted aircraft back into Illinois.

Again, my conclusion that "GAAS" is not entitled to the exemption for the transactions at issue is rather mundane — "GAAS" failed to prove that its agreements to provide retrofit services required it to deliver the goods it transferred incident thereto to its customers outside Illinois. "GAAS's" burden in this regard is elementary to Illinois tax law, and it quite simply failed to provide evidence on this central issue. "GAAS", therefore, has not borne its heavy burden of establishing that Illinois' assessment of SOT here, or that the SOTA itself, is unconstitutional.

Issue 2: Whether "GAAS's" Transfers Pursuant To Its Operating Agreement With "American Signcraft" Are Subject to SOT

"GAAS" next argues that the Department improperly assessed tax based on its purchase and transfer of goods that it installed on customer's aircraft, and based on its

purchase and transfer of the parts it used to repair "American Signcraft"'s loaner/rental aircraft engines, pursuant to its Operating Agreement with "American Signcraft". Taxpayer's Brief, pp. 21-23. Specifically, "GAAS" argues that the Department "proposes assessing the wrong taxpayer with the wrong tax." Taxpayer's Brief, p. 21. It further asserts that, ""American Signcraft" self-assessed and 'directly paid' tax on the materials transferred incident to the performance of the maintenance agreements. (Stip. Ex. 87). And since "American Signcraft" owed — and paid — Use Tax on the materials in question, there is no basis for assessing [it] with Service Occupation Tax on the transfer of the same property." *Id*., pp. 21-22.

When making these arguments, "GAAS" cites to an Informational Bulletin the Department published in 1991 to notify taxpayers of changes in various Illinois tax laws. Taxpayer's Brief, p. 21 (citing FY 91-45). The changes in Illinois law that the bulletin identified, and which are pertinent to this dispute, were changes to the SOTA and to Illinois' Use Tax Act ("UTA") and Service Use Tax Act ("SUTA"). Specifically, new § 3-75 was added to the UTA, which provided:

> Serviceman Transfer.
> Tangible Personal Property purchased by a serviceman, as defined in Section 2 of the [SOTA], is subject to the tax imposed by this Act when purchased for transfer by the serviceman incidental to the completion of a maintenance agreement.

Ill.Rev.Stat. ch. 120, ¶ 439.3 (West Publishing Co.) (Historical and Statutory Notes) (P.A. 86-1394, eff. Jan. 1, 1991) (*currently* 35 **ILCS** 105/3-75).

Public Act 86-1394 also amended the definition section of the SUTA and the SOTA to include the paragraph that provides, "Tangible personal property transferred incident to the completion of a maintenance agreement is exempt from the tax imposed

pursuant to this Act." P.A. 86-1394, § 3 (eff. Jan. 1, 1991) (*currently* 35 **ILCS** 110/2; 35 **ILCS** 115/2). In sum, pursuant to those statutory changes, Illinois tax law no longer considers a person who purchases goods only as an incident to its purchase of a maintenance agreement to be subject to Illinois use tax or service use tax regarding such goods. 35 **ILCS** 105/3-75; 35 **ILCS** 110/2 (definition of "sale of service"). Under the new scheme, the serviceman who purchases goods for transfer incident to the completion of a maintenance agreement is not subject to SOT on such transfers (35 **ILCS** 115/2), but is instead considered the taxable user of such goods. 35 **ILCS** 105/3-75. The serviceman must pay use tax either to its supplier upon its purchase of such goods, or to the Department, directly. 35 **ILCS** 105/9-10.

"GAAS" clearly knows of these statutory provisions that were in effect during the audit period at issue, since it cites to the Department's 1991 informational bulletin and to the SOTA regulation the Department subsequently promulgated pursuant to those statutory changes. Taxpayer's Brief, p. 21. It also knows that, pursuant to its agreement with "American Signcraft", it was "American Signcraft's" "Exclusive … Factory-Sponsored Service and Support Center" for purposes of providing service pursuant to those maintenance service plans ("MSP's"). Stip. Ex. 80, pp. 1-2 (provisos & ¶ 1), 8 ¶ 7. It further knows that "American Signcraft" supplied "GAAS" with parts that "GAAS" was required to purchase and transfer to customers who purchased "American Signcraft's" MSP's. *Id*., pp. 6-7 ¶ 5(a)-(b).

Both parties refer to SOT regulations adopted after the period at issue when arguing that "GAAS" either is or is not subject to use tax on these MSP and loaner/rental engine repair transactions. Those regulations describe a situation in which a serviceman

enters into an agreement with a customer to provide services, and it then hires another serviceman or other servicemen to perform some or all of the service work it has contracted to perform for the customer. In such situations, the former is described as the primary serviceman and the latter are described as secondary servicemen. The regulations all address a situation where the secondary serviceman transfers goods to the primary serviceman, incident to its sale of service to the primary. Thereafter, the primary serviceman transfers the goods (it received from the secondary) to his customer, incident to its sale of service to the customer. 35 **ILCS** 115/2 (definition of transfer). Under currently applicable SOT regulations, the secondary serviceman may or may not be subject to either use tax ("UT") or to SOT, depending on the relative value of the goods transferred vis-à-vis the value of the secondary's services (i.e., a "de minimus secondary serviceman"), and depending on other factors. 86 Ill. Admin. Code §§ 140.105 – 140.109, 140.145 (2001); 86 Ill. Admin. Code §§ 140.145, 140.301 (1990-2001). The contractual relationship between "American Signcraft" and "GAAS", however, is not like the primary-secondary servicemen relationships described by the applicable regulations.

The relationship between "GAAS" and "American Signcraft" does not involve "GAAS's" sales or transfers of goods to "American Signcraft", incident to "GAAS's" agreement to perform services for "American Signcraft". Stip. Ex. 80, pp. 6-7 ¶ 5(a)-(b). Instead of hiring "GAAS" to transfers goods to it, and which "American Signcraft" would then transfer to others, "American Signcraft" hired "GAAS" to provide services and transfer goods directly to those who purchased maintenance service plans from "American Signcraft". *Id*., pp. 1-2, 6-8 ¶¶ 5, 7; Stip. ¶¶ 99-102. The agreement between "GAAS" and "American Signcraft" was that "GAAS" would purchase, from "American

Signcraft", the goods "GAAS" used when performing services pursuant to those maintenance plans, and then install such goods onto aircraft owned by MSP customers, in Illinois. Stip. Ex. 80, pp. 6-8 ¶¶ 5, 7 & Annex B. "American Signcraft" would then reimburse "GAAS" for its services and expenses — including "GAAS's" parts expenses — based on a variety of factors, including an agreed-upon percentage of the list price of the parts "GAAS" purchased from "American Signcraft". Stip. Ex. 80, Annex B; Stip. ¶ 103. Both "GAAS" and "American Signcraft" acknowledge, in the Operating Agreement, that "GAAS" purchased the Designated "American Signcraft" Engine and General Products that "American Signcraft" supplied it with, on consignment, and that "GAAS" then used by installing them into aircraft owned by MSP customers. Stip. Ex. 80, pp. 6-7 ¶ 5(b), & Annex B. The plain terms of "GAAS's" agreement with "American Signcraft" establish that "American Signcraft" was "GAAS's" vendor of the property that "GAAS" then transferred incident to the completion of a maintenance agreement. 35 **ILCS** 115/3-75.

So, while the regulations do not specifically address a primary-secondary serviceman relationship like the one between "GAAS" and "American Signcraft" here, section 3-75 of Illinois' Use Tax Act ("UTA") nevertheless imposes a tax on servicemen who engage in transactions like the ones "GAAS" performed during the period at issue. 35 **ILCS** 105/3-75. "GAAS" does not dispute that it is a serviceman, and the stipulations and the Operating Agreement clearly show that "GAAS" purchased goods for transfer, in Illinois, incident to the completion of a maintenance agreement. Stip. Ex. 80, pp. 6-8 ¶¶ 5, 7 & Annex B; Stip. ¶¶ 101-105, 107-109. While the maintenance agreement was not between "GAAS" and the customers to whom the goods were transferred, that is not an

express requirement of UTA § 3-75. 35 **ILCS** 105/3-75. On its face, the text of § 3-75 applies to the transactions "GAAS" performed here. Thus, even though I disagree with the basis for the audit's determination that "GAAS" owes use tax on its MSP work (*see* Stip. Ex. 81, p. 3), I agree that "GAAS" is, in fact, subject to use tax on its purchase and use of such property in Illinois.

I turn now to the tax assessed on "GAAS's" purchase and use of goods incident to the maintenance and repair work it performed on "American Signcraft"'s loaner/rental engines in Illinois. Stip. ¶¶ 23(c), 107-111. "American Signcraft" hired "GAAS" to perform maintenance and repairs of "American Signcraft"'s loaner/rental engines, which "GAAS" kept in Illinois to rent to customers while providing services to them. Stip. Ex. 80, pp. 11-12 ¶ 11; Stip. ¶ 107. "American Signcraft" supplied "GAAS" with the parts "GAAS" used when maintaining and/or repairing those loaner/rental engines. *Id*.; Stip. ¶ 108. And by "supplied" I mean, again, that "American Signcraft" sold to "GAAS" the parts "GAAS" used when performing the maintenance/repair work. Stip. Ex. 80, pp. 11-12 ¶ 11 & Annex B. "American Signcraft" then reimbursed "GAAS" for that work, using the same formula, and following the same claim procedures, "GAAS" used to claim reimbursement for performing the MSP work. Stip. ¶ 109. The loaner/rental engine maintenance provision of the Operating Agreement, therefore, constitutes a maintenance agreement between "American Signcraft", as the purchaser/customer, and "GAAS", as the serviceman. Thus, the cost price of the engine parts that "GAAS" purchased from "American Signcraft" and installed in "American Signcraft"'s loaner/rental engines, in Illinois, constitutes the base for "GAAS's" own use tax liability. 35 **ILCS** 105/3-75.

I must also reject, for several reasons, "GAAS's" arguments regarding the exemption certificate the parties offered as one of the stipulated exhibits here. Exemption certificates provide an easy way for retailers and servicemen to document that certain gross receipts are not subject to a given occupation tax because they were realized from sales or transfers of goods to exempt purchasers or to purchasers for exempt uses. 35 **ILCS** 120/7; 35 **ILCS** 115/12; American Welding Supply Co. v. Department of Revenue, 106 Ill. App. 3d 93, 435 N.E.2d 761 (5th Dist. 1982); Rock Island Tobacco & Specialty Co. v. Department of Revenue, 87 Ill. App. 3d 476, 409 N.E.2d 136 (3d Dist. 1980). When obtained and kept in good-faith, exemption certificates that are regular on their face satisfy a retailer's or serviceman's burden to provide documentary evidence to support their claim that certain goods were sold or transferred for an exempt use, or to an exempt purchaser. American Welding Supply Co., 106 Ill. App. 3d at 103, 435 N.E.2d at 769 ("we find that the certification procedure designed by the Department to give effect to the statutory exemption places the burden of proving the use of items allegedly purchased … [for exempt use] on the purchaser … rather than on the seller."). To be considered regular on its face, an exemption certificate must: be signed by the purchaser; bear the purchaser's exemption or reseller's identification number; particularly describe the transactions at issue; and it must bear the purchaser's certification that the goods sold or transferred will be used by the purchaser for an exempt purpose, or that the purchaser is, itself, exempt from tax. 86 Ill. Admin. Code § 130.1405(b) (1991-2001).

The exemption certificate "GAAS" produced here does not corroborate its argument that its transfers of goods incident to MSP's were not taxable. First, the plain text of the certificate states that "American Signcraft" was *purchasing* "spare parts …"

from "GAAS". Stip. Ex. 87. That has it perfectly backwards. Under the Operating Agreement, "GAAS" was the purchaser and "American Signcraft" was the seller, under consignment, of the goods "American Signcraft" supplied to "GAAS" for MSP work and for loaner/rental engine repairs. Stip. Ex. 80, pp. 6-8 ¶¶ 5, 7, pp. 11-12 ¶ 11 & Annex B thereto. "GAAS's" documented purchases of the goods it used when performing such service work, pursuant to the Operating Agreement, is important because an exemption certificate signed by the seller of goods, and not by the purchaser, is not regular on its face. 86 Ill. Admin. Code § 130.1405 (1991 – 2001).[5]

I want to particularly stress why the exemption certificate's statement that "American Signcraft" was purchasing "spare parts …" from "GAAS" may not be considered a reasonable understanding of the provisions of the Operating Agreement. The Operating Agreement contains an integration clause, in which the parties agreed that, "This agreement and the other agreements and documents referred to herein contain the complete agreement between the parties and supercede any prior understandings, agreements or representations by or between the parties, written or oral, which may have

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[5] I acknowledge that, under the 2001 amendments to SOT regulation 140.145(c), secondary servicemen are supposed to obtain an exemption certificate from their primary serviceman, but that, again, is pursuant to circumstances in which a secondary serviceman actually transfers goods incident to its sales of service to a primary serviceman. Nothing within that regulation grants a secondary serviceman that does not, in fact, sell or transfer goods to the primary, the right to obtain, and then claim to "rely" on, a sworn certification from the primary that contains what the secondary knows is a clear misstatement of fact.

"GAAS" argues here that, "because "American Signcraft" swore that it already paid Use Tax on the property in question, and because ["GAAS"] had no reason for questioning "American Signcraft"'s claim, there is no basis for seeking [tax] from [it]." Taxpayer's Brief, p. 23. But "GAAS" had every reason to question "American Signcraft"'s claim that it was purchasing "spare parts …" from "GAAS". It knew, pursuant to the express terms of its Operating Agreement, that that was not true. Stip. Ex. 80, pp. 6-8 ¶¶ 5, 7 & Annex B thereto. The reason why it is not appropriate for "GAAS" to take an exemption certificate from "American Signcraft" (*see* Taxpayer's Brief, p. 23) is because, as a matter of black letter Illinois law, exemption certificates are given by purchasers to a seller, and not vice-versa. Rock Island Tobacco, 87 Ill. App. 3d at 6, 409 N.E.2d 136; 86 Ill. Admin. Code § 150.1405.

related to the subject matter hereof in any way." Stip. Ex. 80, p. 20 ¶ 18(g). The parties also agreed that they could amend the terms of the Operating Agreement, "so long as any such amendment … is set forth in a writing executed by each party hereto." Stip. Ex. 80, p. 20 ¶ 18(a). Since only "American Signcraft" signed the exemption certificate, that writing cannot be considered an amendment of the Operating Agreement. *Id*. Nor can the exemption certificate be considered a supplementation of the integrated Operating Agreement. *See* J & B Steel Construction v. C. Iber & Sons Inc., 162 Ill. 2d 265, 273, 642 N.E.2d 1215, 1220 (1994) (where an agreement does not contain an integration clause, supplementation by additional, consistent terms is allowed). As the Illinois Supreme Court impliedly acknowledged in J & B Steel, integrated contracts may not be supplemented, because the parties have unambiguously manifested their agreement that a particular writing sets forth their entire agreement. *Id*.

And even if the Operating Agreement was not integrated, "American Signcraft"'s unilateral and subsequent written statement that it was purchasing "spare parts …" from "GAAS" is simply not consistent with the express provisions of the Operating Agreement. "American Signcraft" sold engine parts and general products to "GAAS", which "GAAS" then either resold to others or transferred to others as an incident to performing repair services. Stip. Ex. 80, pp. 6-8 ¶¶ 5-7, pp. 11-12 ¶ 11 & Annex A-B thereto. Pursuant to ¶ 7 of the Operating Agreement, "American Signcraft" hired "GAAS" to perform services for its eligible customers under the provisions of "American Signcraft"'s MSP's. Stip. Ex. 80, p. 8 ¶ 7. "GAAS" performed those services not as "American Signcraft"'s agent, but as an independent contractor. Stip. Ex. 80, p. 20 ¶ 18(d). The effect of those provisions is that, when it performed MSP work, "GAAS" —

and not "American Signcraft" — owned the engine parts "GAAS" installed into aircraft owned by "American Signcraft"'s eligible MSP customers. Thus, "GAAS" — and not "American Signcraft" — transferred those parts to the eligible MSP customer, even though the customer's contract for maintenance services was with "American Signcraft". 35 **ILCS** 115/2 (definition of transfer).

This conclusion is also consistent with the commonly understood definitions of the words "purchase" and "reimburse," and the parties' own use of those distinct words in the Operating Agreement. "Purchase" means "The act or an instance of buying … Something bought … Acquisition through the payment of money or its equivalent …." and "reimburse" means "To repay (money spent); refund … To pay back or compensate (another party) for money spent or losses incurred." The American Heritage Dictionary of the English Language (4th Ed. 2000) (Houghton Mifflin Company) (available at www.dictionary.com). When the parties to the Operating Agreement wanted to objectively convey that one party was to purchase goods from another, they used the word "purchase." Stip. Ex. 80, pp. 6-8 ¶¶ 5-7, & Annex A. When the parties wanted to objectively convey that "American Signcraft" would reimburse "GAAS" for the work it did for "American Signcraft's" customers, they used the words "reimburse" and "reimbursement." Stip. Ex. 80, p. 8 ¶ 7 & Annex B. In Annex B of the Operating Agreement, the parties further provided that "American Signcraft's" reimbursement would be based, in part, on the costs "GAAS" incurred when it purchased parts used to perform services for "American Signcraft". Stip. Ex. 80, Annex B. Clearly, the parties did not view "American Signcraft's" express agreement to reimburse "GAAS" as constituting the parties' unwritten agreement that "American Signcraft" was really

purchasing the engine parts it had previously sold to "GAAS" on consignment, and then transferring title to those parts to the MSP customer. In short, "reimburse," does not mean "purchase," the parties to the Operating Agreement did not manifest an agreement that, to them, the word "reimburse" meant "purchase," and I will not construe "reimburse" to mean "purchase," either.[6]

Additionally, the certificate admitted as exhibit 87 does not identify any of the transactions at issue in this matter. "American Signcraft's" Senior Tax Accountant, William R. Chipps, signed the exemption certificate on 2/27/98. Stip. Ex. 87. The text of the certification provides that "[t]his certificate *shall be part of each order which we may hereafter give to you,* unless otherwise specified, and shall be valid until canceled by us in writing or revoked by the city or state." Stip. Ex. 87 (emphasis added). The audit period, however, ended on May 31, 1996. Stip. ¶ 2. On its face, therefore, the certificate does not describe any transactions undertaken during the months at issue. Thus, it cannot have satisfied "GAAS's" burden to provide documentary evidence to support its claim that the transactions at issue in this case were not taxable. 35 **ILCS** 120/7; 35 **ILCS** 115/12; 86 Ill. Admin. Code § 130.1405 (1991 – 2001); *see also* Rock Island Tobacco & Specialty Co., 87 Ill. App. 3d at 478, 409 N.E.2d at 138 (Department properly gave no effect to exemption certificates claiming that purchaser bought goods from seller on a date before purchaser commenced business).

"GAAS" also claims that the exemption certificate proves that "American Signcraft" paid the tax in this matter. Taxpayer's Brief, p. 21. It does no such thing. The

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[6] Or, to put it another way, the title trail for the engine parts "GAAS" used when completing MSP work did not flow from "American Signcraft" to "GAAS", then back to "American Signcraft" and then to "American Signcraft"'s eligible customer. Rather, it flowed from "American Signcraft" to "GAAS" to customer. Stip. Ex. 80, pp. 6-8 ¶¶ 5-7, & Annex A-B.

function of an exemption certificate is to provide a seller or transferor of goods with documentary evidence that tends to show that *it* was not subject to an occupation tax regarding a given transaction. *See, e.g.* 35 **ILCS** 120/2c. The fundamental fact established by the seller or transferor's tender of an exemption certificate, however, is that *tax has not been paid*. "GAAS's" argument that its introduction of an exemption certificate proves just the opposite cannot be supported.

Even more fundamentally, Illinois law provides many different types of exemptions from what is colloquially known as "sales tax." For example, there are exemptions for sales or transfers for resale (35 **ILCS** 115/12 (incorporating 35 **ILCS** 120/2c)), for sales or transfers to purchasers for exempt uses (e.g., 35 **ILCS** 115/3-5(5), (7)-(8); 35 **ILCS** 110/2-5(4), (21)-(22)), or for sales or transfers to particular purchasers (35 **ILCS** 115/3-5(2)-(3); 35 **ILCS** 120/(8)-(9)). But no statutory exemption exists for sales or transfers of goods to a purchaser who claims that it will "directly pay the tax" that Illinois law imposes on the seller or the transferor. *See* 35 **ILCS** 115/3-5; 35 **ILCS** 120/2-5. And that is the final reason why the exemption certificate here is not regular on its face — it asserts no exemption authorized by Illinois law. 86 Ill. Admin. Code § 130.1405 (1991 – 2001). I give no more recognition to "American Signcraft's" out-of-court statement that it was "directly paying the tax" than I do to "American Signcraft's" out-of-court statement that it was purchasing the goods at issue from "GAAS". Stip. Ex. 87.

Issue 3: Did The Department Improperly Calculate The Amount of Tax Due Regarding "GAAS's" Purchases and Transfers of Goods When Performing MSP Work, And When Performing Maintenance/Repairs On "American Signcraft's" Loaner/Rental Engines

"GAAS" finally argues that the Department improperly calculated the tax due for the MSP and loaner/rental engine repair transactions. Taxpayer's Brief, pp. 24-26. It asserts that, since "[t]he auditor indicated that ["GAAS's"] invoices for MSP work and rental engine repairs do not segregate the selling price of the materials transferred … the auditor should have simply calculated the proposed tax based on fifty percent of the total invoice amount." Taxpayer's Brief, p. 24. The Department responds that it properly measured SOT here. The Department is correct.

Section 3-10 of the SOTA provides, in pertinent part:

> Rate of tax. Unless otherwise provided in this Section, the tax imposed by this Act is at the rate of 6.25% of the "selling price", as defined in Section 2 of the Service Use Tax Act, of the tangible personal property. **For the purpose of computing this tax, in no event shall the "selling price" be less than the cost price to the serviceman of the tangible personal property transferred.** The selling price of each item of tangible personal property transferred as an incident of a sale of service may be shown as a distinct and separate item on the serviceman's billing to the service customer. If the selling price is not so shown, the selling price of the tangible personal property is deemed to be 50% of the serviceman's entire billing to the service customer. ***
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35 **ILCS** 115/3-10 (emphasis added).

"GAAS's" argument is, in effect, that where a serviceman does not segregate its cost price on its invoices, and where the serviceman's cost price of the goods it transfers incident to its sales of service is greater than 50% of its invoice price, § 3-10 requires the Department to ignore the serviceman's true cost price, and thereby reduce the

serviceman's tax liability. Of course, such a reading completely eviscerates the legislative intent that, "For the purpose of computing this tax, in no event shall the 'selling price' be less than the cost price to the serviceman of the tangible personal property transferred." 35 **ILCS** 115/3-10. Since I trust that the legislature meant what it clearly said, I reject "GAAS's" argument. The Department discerned "GAAS's" cost price of the goods it purchased from "American Signcraft" and installed into others' aircraft in Illinois, and into "American Signcraft's" loaner/rental engines in Illinois, and it properly based "GAAS's" tax liability on the true cost price of such goods.

Conclusion

I conclude that the stipulated record does not establish that the agreements pursuant to which "GAAS" provided retrofit services required it to deliver the goods transferred incident to its sales of service to its customers outside Illinois. Since "GAAS", a serviceman, purchased goods for transfer incident to the completion of a maintenance agreement, it was obliged to pay use tax either to its supplier, "American Signcraft", or to the Department. "GAAS" is also liable for use tax regarding its purchase of engine parts to perform maintenance work on "American Signcraft's" loaner/rental engines in Illinois. The post-dated exemption certificate in which an "American Signcraft" employee swore that it was purchasing goods from "GAAS", and that it was "directly paying the tax," does not prove that "American Signcraft" paid use tax regarding the goods it sold to "GAAS". Nor does that certificate apply on its face to any transactions at issue in this dispute. Finally, the Department correctly measured the amount of applicable tax due regarding the MSP work and loaner/rental engine repairs "GAAS" performed in Illinois.

I recommend, therefore, that the Director finalize the NTL and assessment as issued, with interest to accrue pursuant to statute.

Date: 5/19/2003

John E. White
Administrative Law Judge